

## Assembly Bill No. 2191

### CHAPTER 230

An act to amend Sections 24950, 24953, 25100, 25101, 25111, 25112, 25113, 25114, and 25115 of the Education Code, to amend Section 12420.2 of the Government Code, and to amend Section 770.3 of the Insurance Code, relating to public employees.

[Approved by Governor August 1, 2008. Filed with  
Secretary of State August 1, 2008.]

#### LEGISLATIVE COUNSEL'S DIGEST

AB 2191, Mullin. Public employees: annuities.

Existing law prohibits state and local agencies from negotiating life and disability insurance or requiring the placing of that insurance through particular agents, brokers, or companies, except to the extent that the state has a direct financial interest in the subject of the insurance, as specified. Existing law excepts from these provisions a tax-sheltered annuity under an annuity plan that meets the requirements of Section 403(b) of the Internal Revenue Code to be placed or purchased for an employee, as specified. Existing law permits the Controller to purchase annuity contracts for permanent employees of specified state entities, and requires the Controller to install and operate a uniform state payroll system, as specified. Existing law requires an annuity contract and custodial account as described in Section 403(b) of the Internal Revenue Code to be offered to all employees of any state agency who are members of the State Teachers' Retirement Plan. The Teachers' Retirement Law provides a registration process for information relating to tax-deferred retirement investment products.

This bill would revise the authority of the Controller to purchase annuity contracts for employees of state entities, as described above, to specify that this authority may be exercised on behalf of any state employer under the uniform state payroll system, excluding the California State University System, that employs persons eligible to participate in an annuity contract and custodial account as described in Section 403(b) of the Internal Revenue Code of 1986. The bill would require the Teachers' Retirement Board of the State Teachers' Retirement System to offer an annuity contract and custodial account as described in Section 403(b) of the Internal Revenue Code to eligible state employees of a state employer under the uniform state payroll system, excluding the California State University System, as described above. The bill would make the registration process for information relating to tax-deferred retirement investment products applicable to eligible state employees of these employers. The bill would make various conforming changes.

*The people of the State of California do enact as follows:*

SECTION 1. Section 24950 of the Education Code is amended to read: 24950. (a) An annuity contract and custodial account as described in Section 403(b) of the Internal Revenue Code of 1986 shall be offered to :

(1) All employees of any state agency who are members of the plan under this part.

(2) Any employee of a local public agency or political subdivision of this state that employs persons to perform creditable service subject to coverage by the plan under this part.

(3) Any state employee of a state employer under the uniform state payroll system, excluding the California State University System, eligible to participate in an annuity contract and custodial account as described in Section 403(b) of the Internal Revenue Code of 1986.

(b) The following criteria shall apply to that annuity contract and custodial account:

(1) The annuity contract and custodial account shall be offered for at least five years.

(2) The annuity contract and custodial account may be administered by a qualified third-party administrator that shall, under agreement with the system, provide custodial, investment, recordkeeping, or administrative services, or any combination thereof. The third-party administrator may not provide investment options other than pursuant to a shareholders' services agreement between the third-party administrator and the investment manager.

(3) The investment options offered shall be determined by the board consistent with those annuity contract and custodial accounts described in Section 403(b) of the Internal Revenue Code of 1986.

(4) The system's investment staff shall make recommendations to the board as to the appropriate investment options. At a minimum, the board shall offer at least three investment options. The board shall have sole responsibility for the selection of service providers.

(5) All contributions made in accordance with the provisions of Section 403(b) of the Internal Revenue Code of 1986 and this section shall be remitted directly to the administrator and held by the administrator in a custodial account on behalf of the employee. Any investment gains or losses shall be credited to those accounts. The forms of payment and disbursement procedure shall be consistent with those generally offered by similar annuity contracts and custodial accounts and applicable federal and state statutes governing those contracts and accounts.

(6) Any employer, other than the state, may elect to make contributions to the employee's annuity contract and custodial account on behalf of the employee. The employer shall take whatever action is necessary to implement this section, including the adoption of an annuity contract and custodial account, or provide the appropriate authorization in accordance with the provision of Section 403(b) of the Internal Revenue Code of 1986. Employer contributions made under this section are excluded from the definition of creditable compensation as provided in Section 22119.2.

(7) The design and administration of the annuity contract and custodial account shall comply with the applicable provisions of the Internal Revenue Code of 1986 and the Revenue and Taxation Code. Section 770.3 of the Insurance Code shall not be applicable.

SEC. 2. Section 24953 of the Education Code is amended to read:

24953. (a) For purposes of this section, the following definitions shall apply:

(1) “Annuity contract” means an annuity contract described in Section 403(b) of the Internal Revenue Code that is available to employees as described in Section 770.3 of the Insurance Code.

(2) “Custodial account” means a custodial account described in Section 403(b)(7) of the Internal Revenue Code.

(3) “Third-party administrator” means a person or entity other than the system that provides administrative or compliance services to the system as described in subdivision (b).

(b) An employer that employs persons to perform creditable service subject to coverage by the plan under this part, or the Controller on behalf of any state employer under the uniform state payroll system, excluding the California State University System, that employs persons eligible to participate in an annuity contract or custodial account as described in Section 403(b) of the Internal Revenue Code of 1986, may enter into a written contract with the system for services regarding an annuity contract and custodial account provided by the employer. That contract may include any of the following:

(1) Services to ensure compliance with Section 403(b) of the Internal Revenue Code regarding the annuity contract and custodial account including, but not limited to, services that permit the system to do any of the following:

(A) Administer and maintain written plan documents governing the employer’s plan.

(B) Review and authorize hardship withdrawal requests, transfer requests, loan requests and other disbursements permitted under Section 403(b) of the Internal Revenue Code.

(C) Review and determine domestic relations orders as qualified domestic relations orders as described in Section 414(p) of the Internal Revenue Code.

(D) Provide notice to eligible employees that is consistent with Title 26 of the Code of Federal Regulations that those employees may participate in an annuity contract and custodial account.

(E) Administer and maintain specimen salary reduction agreements for the employer and employees of that employer to initiate payroll deferrals.

(F) Monitor, from information provided either directly from the employee, as part of the common remitting services provided pursuant to paragraph (2), through information provided by the employer, or through information provided by vendors authorized by the employer to provide investment products, the maximum contributions allowed by employees participating in the annuity contract and custodial account as described in Sections 402(g), 414(v), and 415 of the Internal Revenue Code.

(G) Calculate and maintain vesting information for contributions made by the employer to the annuity contract and custodial account.

(H) Identify and notify employees that are required to take a minimum distribution of the funds in that employee's annuity contract and custodial account as described in Section 401(a)(9) of the Internal Revenue Code.

(I) Coordinate responses to the Internal Revenue Service if there is an Internal Revenue Service audit of the annuity contract and custodial account.

(2) Services to administer the annuity contract and custodial account that include, but are not limited to, all of the following:

(A) Common remitting services.

(B) General educational information to employees about the annuity contract and custodial account that includes, but is not limited to, the enrollment process, program eligibility, and investment options.

(C) Internal reports for the employer to ensure compliance with Section 403(b) of the Internal Revenue Code and Title 26 of the Code of Federal Regulations.

(D) Consulting services related to the design, operation, and administration of the plan.

(E) Internal audits, on behalf of an employer, of a provider's plan compliance procedures with respect to the provider's annuity contract and custodial account offered under the employer's plan. These audits shall not be conducted more than once per year for a provider's plan, unless documented evidence indicates a problem in complying with Section 403(b) of the Internal Revenue Code.

(c) If the system elects to contract with a third-party administrator for the administrative or compliance services to employers described in subdivision (b), the system shall do all of the following:

(1) Determine that hiring the third-party administrator is in the best interest of the participants to the annuity contract and custodial account, their beneficiaries, and the employer that provides that annuity contract and custodial account.

(2) Require the third-party administrator to provide proof of liability insurance and a fidelity bond in an amount determined by the system to be sufficient to protect the assets of participants and beneficiaries in the annuity contract and custodial account.

(3) Require evidence, if the third-party administrator is related to or affiliated with a provider of investment products pursuant to Section 403(b) of the Internal Revenue Code, that data generated from the services provided by the third-party administrator are maintained in a manner that prevents the provider of investment products from accessing that data.

(d) Any personal information obtained by the system in providing services pursuant to this section shall be used by the system only to provide those services for the employer in accordance with the contract entered into with the employer pursuant to subdivision (b).

(e) Nothing in this section requires an employer to contract with the system for the administrative or compliance services described in subdivision (b). A written contract for the administrative or compliance services

described in subdivision (b) shall be on behalf of and at the request of the employer.

(f) Nothing in this section shall be construed to interfere with either:

(1) The rights of employees or beneficiaries as described in Section 770.3 of the Insurance Code.

(2) The ability of an employer to establish nonarbitrary requirements upon providers of an annuity contract that, in the employer's determination, aid in the administration of its benefit programs and do not unreasonably discriminate against any provider of an annuity contract or interfere with the rights of employees or beneficiaries as described in Section 770.3 of the Insurance Code.

(g) The cost of providing administrative or compliance services pursuant to this section shall be deemed to be a cost incurred by the employer and subject to subdivision (b) of Section 44041 or subdivision (b) of Section 87040, as may be applicable.

(h) In any conflict between this section and Section 44041.5 or 87040.5, including, with respect to the provision of services provided pursuant to a contract between an employer and the system, the provisions of this section shall prevail.

(i) The system shall disclose to an employer seeking the services described in this section any fees, commissions, cost offsets, reimbursements, or marketing or promotional items received by the system or a third-party administrator from any plan provider selected as a vendor of an annuity contract or custodial account by the employer. If the system or a third-party administrator is affiliated with or has a contractual relationship with a provider of annuity contracts or custodial accounts, the system or third-party administrator shall disclose the existence of that relationship to each employer and employee participating in the annuity contract or custodial account.

SEC. 3. Section 25100 of the Education Code is amended to read:

25100. (a) The board shall establish a vendor registration process through which information about tax-deferred retirement investment products as described in Section 403(b) of the Internal Revenue Code of 1986 shall be made available for consideration by public employees of all local school districts, community college districts, county offices of education, and state employees of a state employer under the uniform state payroll system, excluding the California State University System, eligible to participate in an annuity contract and custodial account as described in Section 403(b) of the Internal Revenue Code of 1986.

(b) For the purposes of this chapter, "403(b) product or 403(b) products" means tax-deferred retirement investment products as described in Section 403(b) of the Internal Revenue Code of 1986, and its subsequent amendments, and complying with applicable California insurance laws, and federal and California securities laws and rules as applied by appropriate regulatory entities.

(c) For the purposes of this chapter:

(1) “Employer” means any local school district, community college district, or county office of education, or any state employer under the uniform state payroll system, excluding the California State University System, with employees eligible to participate in an annuity contract and custodial account as described in Section 403(b) of the Internal Revenue Code of 1986, with the Controller acting on the state employer’s behalf.

(2) “Vendor” means a public retirement system, broker-dealer, registered investment company, nonbank custodian, or life insurance company qualified to do business in California that provides 403(b) products. “Vendor” does not include individual registered representatives, brokers, financial planners, or agents.

(3) “Nonbank custodian” means a fund custodian, other than a bank, that meets the criteria of a trustee specified in Section 408(a)(2) of the Internal Revenue Code.

(4) “Broker-dealer” means only those broker-dealers who offer a proprietary 403(b) product or who charge fees that are otherwise not disclosed.

SEC. 4. Section 25101 of the Education Code is amended to read:

25101. A prospective vendor of 403(b) products that offers those products, or the products of other 403(b) vendors, to employers and their eligible employees, shall register those products with the board pursuant to this chapter. Registered vendors shall offer only registered 403(b) products as funding vehicles for 403(b) plans.

(a) Prospective vendors shall be registered with the board based upon a complete response to the disclosures required by this subdivision. This information shall be included in the impartial investment information bank established pursuant to Section 25104. The prospective vendors shall provide the following information:

(1) A statement of experience in California and in other states in providing retirement annuities, custodial account mutual fund arrangements, or other retirement products and related financial services under public employer retirement plans.

(2) A characterization by the vendor of its offering as either an annuity or custodial account, as defined under Sections 403(b)(1) and 403(b)(7) of the Internal Revenue Code, respectively.

(3) A disclosure of all expenses paid directly or indirectly by retirement plan participants, including, but not limited to, penalties for early withdrawals, declining or fixed withdrawal charges, surrender or deposit charges, management fees, and annual fees, supported by documentation as required for prospectus disclosure by the National Association of Securities Dealers and the Securities and Exchange Commission. Vendors shall be required to provide information regarding the impact of product fees upon a hypothetical investment, as described in Section 25104.

(4) The types of products, product features, including presence of two tier annuity features, services offered to participants, and information about how to access product prospectuses or other relevant product information.

(5) A discussion of the ability, experience, and commitment of the vendor to provide retirement counseling and education services, including, but not limited to, access to group meetings and individual counseling by various means, including telephone and telecommunications devices for the deaf (TDD), Internet, and face-to-face consultations by registered representatives.

(6) A statement of the financial strength and stability of the vendor, as may be applicable, by identifying its ratings assigned by nationally recognized rating services that evaluate the financial strength of life insurance, mutual funds, and other similar companies.

(7) The location of offices and counselors, or method of distribution, of the vendor relative to serving employers and their eligible employees in California.

(8) A description of the ability of the vendor to comply with all applicable provisions of federal and state law governing retirement plans, including minimum distribution requirements and contribution limits.

(9) To the extent applicable, the demonstrated ability of the vendor to offer an appropriate array of accumulation funding options, including, but not limited to, a diversified mix of value, growth, growth and income, hybrid and index funds or accounts across large, mid, and small capitalization asset classes, both domestic and international. These investment products may include mutual funds, group or individual annuity contracts, fixed or variable annuity contracts, individual retirement annuities, interests in trust and collective trusts, separate accounts, and other financial instruments.

(10) A discussion of the range of administrative and customer services provided, including asset allocation, accounting and administration of benefits for individual participants, recordkeeping for individual participants, asset purchase, control, and safekeeping, execution of a participant's instructions as to asset and contribution allocation, calculation of daily net asset values, direct access for participants to their account information, periodic reporting to active participants, not less than quarterly, on their account balances and transactions, and compliance with the standard of care applicable in the provision of investment services and consistent with federal law.

(11) Certification by the vendor that the information provided to the board accurately reflects the provisions of the Section 403(b) products they register pursuant to this chapter.

(b) Registration may not be conditioned upon the content of the information.

(c) Vendors shall supply information and data in the format required by the board.

SEC. 5. Section 25111 of the Education Code is amended to read:

25111. Each employer, in consultation with the exclusive bargaining agent of its employees, if any, may develop a process to ensure that employees are aware of, and have access to, information provided in the impartial investment bank maintained by the board.

SEC. 6. Section 25112 of the Education Code is amended to read:

25112. Personnel, including elected school officials, acting on behalf of an employer, may not receive consideration from a vendor in exchange for the promotion of a particular vendor or vendor's products.

SEC. 7. Section 25113 of the Education Code is amended to read:

25113. An employer may not forward annuity or custodial account consideration to the vendor of any unregistered 403(b) product, except insofar as an employee continues making contributions to an unregistered product or products as described in Section 25114.

SEC. 8. Section 25114 of the Education Code is amended to read:

25114. Except as provided in this section, an employee shall select from registered 403(b) products.

(a) An employee of a local school district, community college district, or county office of education may continue to make contributions to unregistered products purchased or entered into prior to the date of implementation of the impartial investment bank, as established by this chapter.

(b) A state employee of a state employer under the uniform state payroll system, excluding the California State University System, eligible to participate in an annuity contract and custodial account as described in Section 403(b) of the Internal Revenue Code of 1986, may continue to make contributions to unregistered products purchased or entered into prior to January 1, 2009.

SEC. 9. Section 25115 of the Education Code is amended to read:

25115. For purposes of restricting the use of 403(b) investment products provided to eligible employees of employers by those vendors and investment products registered with the board pursuant to this chapter, the provisions of Section 770.3 of the Insurance Code do not apply.

SEC. 10. Section 12420.2 of the Government Code is amended to read:

12420.2. The Controller may purchase annuity contracts on behalf of any state employer under the uniform state payroll system, excluding the California State University System, that employs persons eligible to participate in an annuity contract and custodial account as described in Section 403(b) of the Internal Revenue Code of 1986 provided that all of the following conditions are met:

(a) The annuity contract is under an annuity plan which meets the requirements of subdivision (b) of Section 403 of the Internal Revenue Code.

(b) The employee makes application to the Controller for the purchase and reduction of salary.

(c) All provisions of the Insurance Code applicable to the purchase of those annuities are satisfied.

SEC. 11. Section 770.3 of the Insurance Code is amended to read:

770.3. No state department or agency shall negotiate any life or disability insurance or require the placing of that insurance through particular agents, brokers, or companies, except to the extent that the state has a direct financial interest in the subject of the insurance. The state has no financial interest in an annuity purchased for an employee if the premium therefor is paid

from a deduction from or reduction in the employee's salary, and any annuity paid for through a deduction or reduction shall not be deemed to have been provided by the state for its employees for purposes of this section, and the state shall not negotiate or require the placing of the annuity through particular agents, brokers, or companies. Nothing contained in this section shall affect the program of life and disability insurance in connection with veterans' farm and home purchases through the Department of Veterans Affairs except that the total life insurance benefit under that program shall in no event exceed 120 percent of the unpaid contract balance. Except in those cases where the premium for an annuity is paid entirely from a deduction from or reduction in an employee's salary, nothing contained in this section shall affect life or disability insurance programs which may be provided by the state for its employees.

Notwithstanding anything in this section to the contrary, in any case in which a tax-sheltered annuity under an annuity plan which meets the requirements of Section 403(b) of the Internal Revenue Code of 1954 is to be placed or purchased for an employee, the employee shall have the right to designate the licensed agent, broker, or company through whom the employee's employer shall arrange for the placement or purchase of the tax-sheltered annuity. In any case in which the employee has designated an agent, broker, or company, the employer shall comply with that designation, except in the case of a designation subject to Section 1153 or Section 12420.2 of the Government Code, or Section 24950 of the Education Code.

As used in this section, "state department or agency" shall include, but not be limited to, school districts.

This section shall apply to all local governmental agencies, as well as state departments and agencies.